Statement before the ERISA Advisory Council
On Employee Welfare and Pension Benefit Plans

ISSUE: Managing Disability Risks In An
Environment of Individual Responsibility
August 28, 2012

Introduction:

Thank you for the opportunity to testify on the topic of disability risks in the rapidly changing landscape of employer sponsored benefits. This has been a topic of interest to me personally, as well as an evolving challenge I've dealt with professionally in my 11 years as a Human Resources Executive at Silgan Containers, and my over 30 years in the Human Resources profession. In this testimony, I offer my thoughts and opinions on managing disability risks from the perspective of an employer, and hope that it is helpful to the council as you deliberate on the issue and provide counsel to the Department of Labor about how to bridge the gap in disability coverage inside retirement plans in our country.

Background:

Currently, I am the Vice President, Human Resources for Silgan Containers Corporation headquartered in Woodland Hills, California. Silgan Containers is one of 3 business units of Silgan Holdings, which is headquartered in Stamford, Connecticut. The Containers Human Resources organization provides U.S. based operations with HR services to the Containers business primarily, and similar support for the Silgan White Cap (Closures) and Silgan Plastics businesses with headquarters in Chicago and St. Louis respectively.

Silgan Holdings is a $3.2BB global packaging concern serving the consumer goods packaging markets. The company was founded in 1987 and operates facilities in North and South America, Europe, and the Far East. Global employment is in excess of 7,400.

A large portion of the company's domestic operating locations for all 3 business units (27) are represented by a variety of unions including the IAM, UFCW, USWA, IBT, GMP, Sheet Metal Workers, and ITPE. The company has a number of domestic non-union locations as well (13).

The company offers health and welfare plans as well as DB and DC retirement plans to its employees. The plan offerings include a variety of PPO and high deductible H.S.A. plans, and participation in multi-employer health and DB pension plans for some of the unionized locations.

Statement:

As I believe we all know, and as previous testimony points out with a wide variety of statistics, over the last decades, employer sponsored health and welfare, and retirement plans have undergone a dramatic shift. A variety of economic factors are squeezing companies' margins, resulting in less available money to spend on providing a labor market competitive range of benefits, and making it necessary for Human Resources leaders to think about total rewards and the employee value proposition in a new way. At the level of individual retirement benefits, for example, various financial and demographic factors have led to a shift from Defined Benefit ("DB") to Defined Contribution ("DC") retirement plans. This shift has produced new states of risk and responsibility for individuals, and it has also changed the landscape of disability benefits.

After WWII, DB pension plans became the most common type of retirement plan. In these plans, participants receive a regular monthly payment from the date of retirement until death. DB pension plans are often paid for entirely by the employer (i.e., no participant contributions required), and the employer assumes the risk of investing plan assets to manage future obligations.

DC retirement plans (i.e., 401k) have been rising in popularity in place of DB pension plans. In a DC plan, participants make contributions to individual accounts most likely administered by a third party administrator/record keeper. Through a plan sponsored by an employer, contributions are either deducted from the participant's pay or made by the employer. This is a key difference from the DB plans. Historically, DC plans were offered by smaller firms or as supplemental plans to augment employee retirement savings. Some believe DC plans were not adequately designed to become the predominant retirement plan, yet in recent years, they have become the primary source of retirement benefits for an increasing number of retiring Americans.

There are a number of causes for the shift from DB to DC plans, including philosophical shifts regarding the responsibility of retirement security, increasing costs of DB plans, an increasingly strict regulatory environment around funding DB pension plans, and increased workforce mobility. Demographic changes have increased the cost of DB plans, and interest rate changes have enhanced the financial volatility of funding such plans. As we've seen in the last decade, the PBGC has taken on an enormous burden of failed and failing plans. Many organizations no longer have the ability to bear the heightened costs and risks associated with DB plans, and have been shifting the responsibility of saving for retirement to individuals in addition to the PBGC. As workforce mobility increases, and more workers stay with an organization fewer than five years, employees find some advantage from this shift toward DC plans.

For these reasons, many companies have stopped creating DB plans and have closed existing plans to new entrants. In some cases, DB plans that people counted on for their retirement security have been frozen. As mentioned previously, this movement away from DB plans shifts retirement security responsibility and risk from the company to individuals.

Shifting retirement program responsibility presents employees with both risks and opportunities. Employees will need to continue learning how to manage planning and risk through participation in employer sponsored DC plans; assess and understand contributions rates, asset allocation strategies, and keep learning how to resist the temptation in connection with early account withdraws. Just as employers sponsoring DB plans used to start planning early for retirements, so too, employees are learning the art of planning for their futures as the landscape shifts to a DC world. Silgan is assisting in this regard in thoughtful and exciting ways.

The shift from DB to DC plans has resulted in the need to examine long-term disability ("LTD") benefits. DB plans often included built-in LTD benefits. DC plans do not typically include LTD benefits, but when companies shift to DC plans they may not replace the LTD benefits that were part of the DB plan. Thus, employees participating in a DB pension plan often receive greater LTD benefits than employees not participating in a DB plan. Since the shift from DB to DC plans happens gradually in many organizations, there can be a wide range in the LTD benefits employees receive in a single organization.

In many cases, DB plans provided continued benefit accruals to disabled workers similar to when they were actively employed. This meant that retirement benefits continued to grow through periods of disability, and workers would receive benefits similar to those they would have received absent the disability. DC plans lack similar LTD benefits: often no additional contributions are made to the individual accounts of disabled employees. As a result, disabled participants' retirement security can be compromised if they are not enrolled in a pay continuation plan like STD, or LTD. Additionally, disabled workers can withdraw money from their DC plans early, penalty free, and may have fewer assets remaining in their DC retirement plan when they reach retirement age as a result.

Like many organizations, the transition from DB to DC plans has been gradual for Silgan, which has closed DB plans, and enhanced DC plans. Thus, some disabled participants continue to receive retirement accruals through a DB plan, while others do not. When employees go on disability, Silgan offers salary employees pay continuation at 100% of salary for up to 6 months. Silgan also offers employees voluntary long term disability, which employees can purchase by way of payroll deductions through a carrier (MetLife) at group rate discounts. 70% of eligible employees have enrolled in the plan. Lack of motivation on the part of employees to spend money preparing for an unlikely event can be a barrier to coverage, however.

<u>Options for Consideration</u>:

As an employer, I see a variety of options for providing LTD coverage:

1. Offer LTD coverage through DB pension plans:
   Currently the DB system is too risky and costly to be a viable option for many organizations, thus the market is trending away from these plans. Moreover, discrimination testing applied to DB pension plans can result in employers removing/modifying DB program benefits, rights, and features in order to have plans remain compliant with testing regulations. Sometimes, regulatory requirements, while well intended, can create downside, unintended consequences on plans and therefore plan participants. Closing a DB pension plan can impact discrimination testing (HCE's vs. Non-HCE's) 5 to 7 or more years into the future following the closing of a DB plan, depending on the changing nature of the demographics inside a plan.

2. Offer employer sponsored LTD coverage, perhaps with the option for employees to purchase additional coverage:
   The majority of large employers (53%) still offer employer paid LTD plans. However, many of these companies (22%) are re-structuring this benefit by offering employer paid coverage with a base amount of 40-50% of salary, and allowing employees to purchase additional coverage at a group rate (often up to 60% of salary). Voluntary or employee paid LTD coverage usually has an option to include bonus in the benefit formula and provide coverage to social security normal retirement age.

3. Offer employees the option to purchase LTD coverage through the company:
   This is a growing trend, although still in the minority at 15% of large employers. These companies are eliminating employer paid disability plans and replacing them with employee paid options. This has allowed employers to direct the premium elsewhere (i.e. decrease employee contributions or plan enhancements). This option also allows the employee to pay with pre-tax dollars. Silgan, for example, provides a voluntary employee paid LTD plan that pays 60% of an employee's base pay up to Social Security age.

4. Provide no LTD coverage or assistance:
   This option is not very common among large companies. In a study done by Mercer, 84% of manufacturing companies offer some form of disability benefit to their employees.

5. Provide a vehicle for LTD inside the framework of a 401k Plan:
   401k plans are growing in their sophistication. Some record keepers and employers are forming partnerships around annuity and annuity-like product to add to a program's fund line up. Silgan's plans offer this kind of option to provide participants with a steady stream of income upon retirement. Participants are eligible to trigger payments from this product at age 55. Arguably, this still leaves the period of time, for example, from age 25 to 54 open for debate, but a combination of employee options to purchase an LTD product and participate in this kind of retirement program can continue to move retirement and income security in the direction of an individualized approach. Additionally, increased company matching contributions can provide needed income security for retirement years and provide added

funding support for the LTD set of circumstances. In the context of a total rewards strategy there are ways to increase the efficiencies around deploying total compensation dollars.

6. Be prepared to reconcile any/all ideas with Social Security disability or state disability insurance.

As leaders of organizations assess these options, and decide which role the organization will assume in providing LTD coverage to their workforce, they take the following considerations into mind: being a responsible employer, working within the organization's financial constraints, and using available funds wisely to maximize the employee value proposition; the employer's approach to total rewards.

Maximizing the employee value proposition is a strategic concern as it is critical for attracting and retaining the talent an organization needs to succeed. Many organizations now view the employee value proposition through a comprehensive total rewards lens, which extends beyond compensation and benefits to include all elements of employee health, wealth, and career.

Just as the employment deal between employers and employees has changed regarding risk and responsibility in retirement plans, the employment deal has also changed to include a new emphasis on total rewards (Base + STI + LTI + H&W + Retirement + Career Development = TR). This means that the employment deal now encompasses an increased emphasis on training and development, pay for performance, and health and wellness management. Since the economic downturn, the combination of pay cuts and benefit freezes, reduced training and promotion opportunities, and layoffs that affect remaining employees has led to the debate about a new set of ground rules in connection with an evolving "promise" around a new value proposition. An improved economy could bring talent management more deeply into focus for employers and that concern is not lost on Silgan, nor do I believe it is lost on other employers.

For these reasons, it has never been more important to get the relationship between employers and employees right, and striking a balance between providing an excellent value proposition and working with financial constraints necessitates strategic workforce investments. Strategic investments protect and care for employees but also align with their preferences, allowing employers to offer a more desirable value proposition than their competitors.

Studies about specific elements of the value proposition show a growing concern among workers about benefit costs and choices, and less satisfaction with their current benefits. More and more employees see benefits as a significant consideration to join or continue to work with an organization, and an increasing number of employees are saying that their benefits are unsatisfactory or do not meet their needs. They want more choice in the way their benefit/compensation money is allocated. To address these issues, employers need to be clear about employee preferences, and evaluate and redesign compensation strategies to ensure meaningful choice or improve employee control over the spending of employer subsidy.

LTD is an interesting benefit to view in the context of this total rewards equation. Though most workers will never go on long-term disability, it is of great value to those who do receive it. Employees want/deserve the peace of mind that this benefit affords, but it generally is not at the forefront of their minds when making decisions about where to work. Additionally, few understand or spend time thinking about the implications of long-term disability on retirement security. If dollars spent on LTD benefits would add more value in the eyes of an employee if used elsewhere, then employers have little incentive to spend their limited funds sponsoring those programs. This emphasizes the necessity of designing cost effective ways to act as a responsible employer in the realm of LTD, such as educating employees on the importance of LTD coverage and allowing them to purchase that coverage through the organization. Just as employers have adopted auto-enroll and auto-increase components of their 401k offerings, perhaps it’s time to apply similar concepts to LTD coverage in the context of a DC framework.

If deployment of total rewards dollars becomes the norm, there are some issues to consider around STD and/or LTD. One option could be to reduce the employer paid salary continuation benefit from 6 months to 3 months, and supplement with an employee paid STD plan. Another option is to reduce the weekly benefit to 60% for months 4 - 6. Additionally, employers could offer a voluntary LTD plan with a 40% - 60% monthly benefit to bridge the gap until retirement and Medicare benefits are available.

These are difficult choices to make as an employer because employers want to make responsible choices within a web of constraints. When I think about steps that the DOL can take to change the constraints in this situation and reduce the disability risks that exist, I see three stakeholder groups that the DOL can work with: employers, workers, and insurers. I also conceive of two main strategies the DOL can employ with these stakeholders encouraging coverage, and incentivizing coverage.

Encourage the stakeholders mentioned above to supply or obtain adequate coverage. There are steps the DOL can take to support employers in offering better coverage and to persuade employees to ask for better coverage (making it a more important element of the value proposition). There are many potential educational possibilities, campaigns, and opportunities to make creative tools and resources (online, etc.) available to facilitate access to coverage. Encouraging employers and employees to think about LTD coverage through education will motivate insurers to expand their product offerings to meet their clients’ demands.

Portability is a consideration, given the increasingly mobile workforce. When employers pay for LTD coverage it is typically through a group plan with limited or no portability, meaning employees do not have the option to maintain the coverage when they change employers. This can be detrimental if the individual's new employer does not provide LTD coverage. If group coverage could be structured to more feasibly facilitate portability, this could limit the number of individuals who lose coverage when changing jobs. While individual insurance policies are typically portable, currently it is very difficult for workers to get an individual disability policy due to pricing, underwriting, and exclusions. Potential insurance solutions include providing an exchange where employers can send employees to purchase individual disability policies.

Another relevant option is to incentivize organizations and individuals to offer and obtain better disability coverage which would be a powerful way to address the current gaps in the system. As I've discussed, organizations currently have little incentive to direct valuable portions of their total reward spend towards disability benefits if that's not what employees see as valuable. Monetary changes to the equation, such as tax incentives, change the rules of the game and could be a powerful motivator for employers and insurance companies to shift the weight of their offerings.

Concluding Remarks:

In view of the above I believe our global challenges are two-fold; infrastructure and education. Government and the employment sector (both private and public) representatives need to continue collaborating to identify creative solutions in an environment of self reliance and individual success. No single entity can provide the answers to all questions. The dollars it takes to do that are simply not available. However, evolving the 401k concept in connection with; or in partnership with the need for employers to re-think their value propositions and their approach to total rewards, I believe, can position working Americans for increased income security. I believe people will welcome such an approach and will embrace an evolution that supports their individual needs vs. a collective one-size-fits-all approach. Let's enable and celebrate individuality and independence. That's what made us. That's what will keep us.

Thank you for the opportunity to testify on this important topic. I look forward to continuing to work with you, and I will be happy to take your questions.

Sincerely,

Tony Cost